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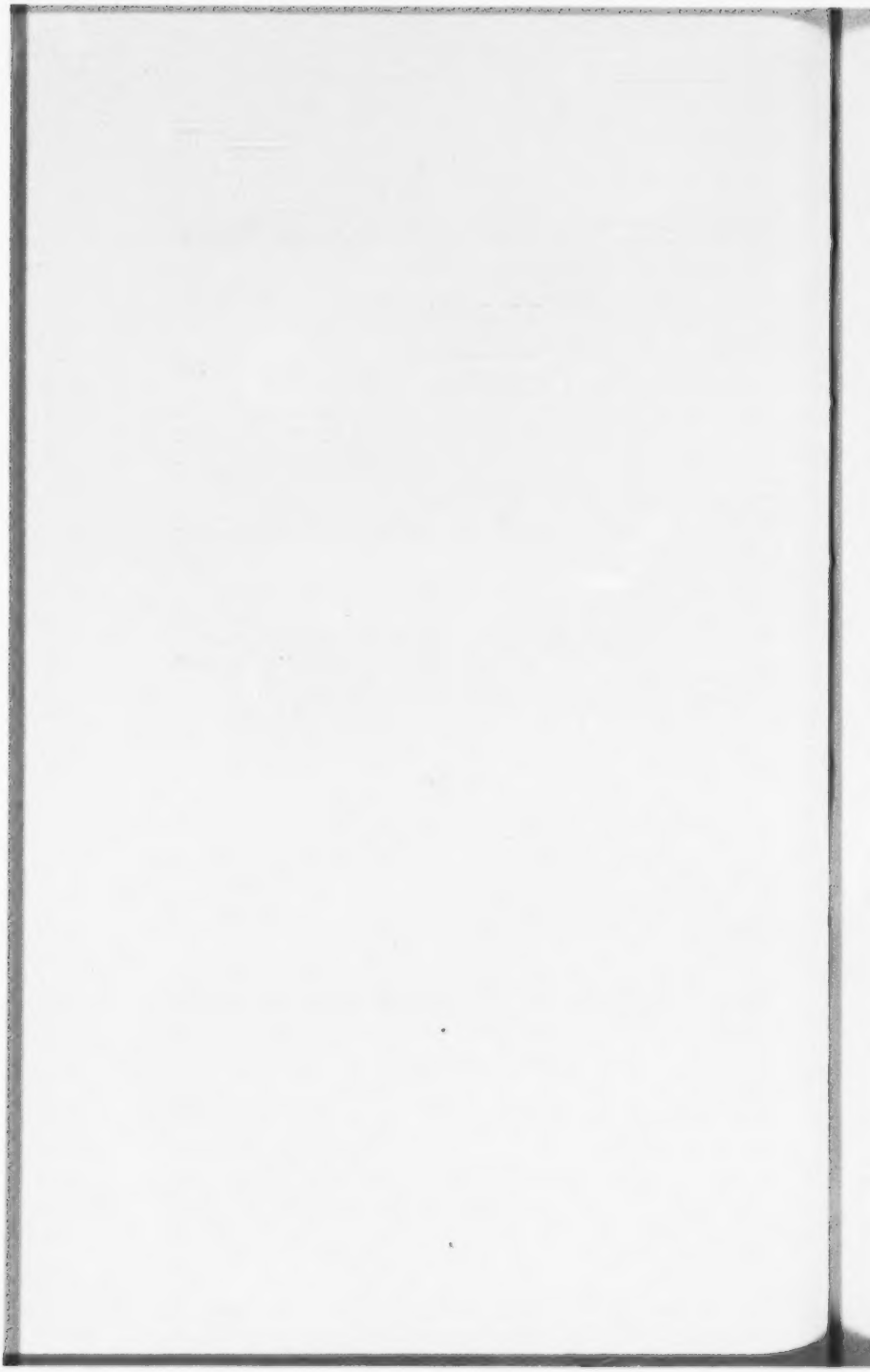

In the Supreme Court of the United States

OCTOBER TERM, 1941

No. 624

MARRS MCLEAN, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the United States Board of Tax Appeals (R. 179–204) is reported at 41 B. T. A. 565. The opinion of the United States Circuit Court of Appeals (R. 346–352) is reported at 120 F. (2d) 942.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 20, 1941 (R. 352). The petition for a writ of certiorari was filed September 17,

1941. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the bonus and oil payments which the taxpayer received pursuant to a contract of assignment of certain oil and gas leases, subject to royalties reserved to himself, were, as the Commissioner contends, ordinary income or, as the taxpayer contends, proceeds derived either from the sale or exchange of capital assets, within the meaning of Section 101 of the Revenue Acts of 1928 and 1932 and Section 117 of the Revenue Act of 1934, or from the "sale of mines, oil or gas wells" or of "any interest therein," within the meaning of Section 102 of the Revenue Acts of 1928 and 1932.

STATUTES INVOLVED

These will be found in the Appendix, *infra*, pp. 6–9.

STATEMENT

The facts were stipulated (R. 212–338) and found by the Board as stipulated (R. 182). They may be summarized as follows:

The taxpayer and his wife are residents of Texas and all of their income is community income. They filed separate income-tax returns for each of the taxable years 1930 to 1935, and they kept their books and reported their income during those years upon a cash basis. (R. 182–183.)

In 1919 the taxpayer and his wife leased lands situated in Galveston County, Texas, for the exploration and production of oil, gas, and other minerals. These leases provided for the payment of a one-eighth royalty to the lessors. (R. 183.) Before March 18, 1931, taxpayer and his wife had discovered oil and developed oil production in commercial quantities upon the leased premises. The principal value of the leases was demonstrated by the prospecting, exploration, and discovery work thus done by the taxpayer and his wife. (R. 183, 215.)

On March 18, 1931, taxpayer transferred and assigned the leases to the Yount-Lee Oil Company in consideration of a cash payment of $500,000 and an oil payment of $2,000,000 to be paid out of one-eighth of all oil and gas produced from the lands subject to the leases. In addition, the taxpayer reserved and excepted from the assignment a royalty of twenty-five percent of all the oil produced; it was agreed that the one-eighth base royalty of the landowners was to be paid out of this twenty-five percent royalty. (R. 183–185.)

In their income-tax returns for the years 1931 to 1935, inclusive, the taxpayer and his wife reported the cash and the oil payments made under this contract as proceeds from the sale of capital assets and the royalty payments as ordinary income (R. 186, 223). The Commissioner determined that all the payments constituted ordinary

income and determined deficiencies accordingly (R. 22–31, 74–78, 95–114, 130–139). The Board of Tax Appeals upheld the Commissioner's determination (R. 204–205) and the court below affirmed (R. 352).

ARGUMENT

The transaction here is, as the court below held (R. 350–351), substantially identical with that involved in *Palmer* v. *Bender,* 287 U. S. 551. There, as in this case, the taxpayer assigned an oil and gas lease in return for a cash bonus, an oil payment, and a royalty. This Court held that, because of the retention of the royalty and oil payment interest, the assignment could not be treated as a sale and that, therefore, the taxpayer was entitled to a depletion allowance. That ruling is decisive of the present case. It cannot be distinguished on the ground that it involved the question whether the assignor of the lease was entitled to a depletion allowance rather than whether the assignor realized ordinary income; as this Court pointed out in *Anderson* v. *Helvering,* 310 U. S. 404, 407, "the same basic issue determines both to whom income derived from the production of oil and gas is taxable and to whom a deduction for depletion is allowable." In view of the recent reaffirmance of the principle of *Palmer* v. *Bender* in the *Anderson* case, there is no occasion for further consideration of the issue in this case.

CONCLUSION

The case was decided by the court below in accordance with the controlling decisions of this Court. There is no conflict. The petition should therefore be denied.

Respectfully submitted.

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OCTOBER 1941.